Educational

Monetary Policy Instruments used by the CBN

Until about 1993 when OMO was introduced, the CBN relied almost exclusively on varying combinations of direct instruments of monetary control from time to time. These instruments included: credit ceilings, sectoral credit allocation, interest rate controls, imposition of special deposits, moral suasion, movement of government deposits, stabilisation securities and exchange contols, etc. As the financial markets deepened over time as a consequence of the economy-wide macroeconomic reforms that commenced mid 1980s, the CBN started the process of shifting from the use of direct instruments to market-based instruments. The most significant move in the new direction came in June 1993 when the Bank introduce OMO. The market-based tools include in addition to OMO, reserve requirements which specifies the proportion of a bank's total deposit liabilities that should be kept with the central bank; and discount window operations under which the central bank performs the role of lender of last resort to the deposit money banks. Open market operations may be undertaken through outright transactions or through repurchase transactions. Repurchase transactions are temporary and are usually reversed at the expiration of the contract. Where a party purchases securities and gives out cash with agreement to sell the securities back at a later date with some financial consideration a repo agreement is in place. On the other hand if securities have been sold to a party and cash taken with agreement to purchase the securities at a later date with some interest, a reverse repo transaction is deemed to be in place. Currently, OMO is the major instrument of monetary policy at the CBN. Other supporting instruments are discount window operations, moral suasion, forex sales and the standing facility introduced in December 2006.